

## Message Text

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C O N F I D E N T I A L PEKING 1977

LIMDIS

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SUBJECT: FERROUS SCRAP

REF: A) STATE 196158 B) STATE 240711 C) STATE 242766

SUMMARY: IN RESPONSE TO AN EXPLANATION BY USLO OFFICER ABOUT FOURTH QUARTER STEEL SCRAP ALLOCATIONS FOR THE PRC, AN OFFICIAL OF THE CHINESE METALS AND MINERALS CORPORATION TOOK A STRONG POSITION ON THOSE CONTRACTS WHICH WERE NOT FULFILLED BY US FIRMS DUE TO THE IMPOSITION OF US EXPORT CONTROLS AT THE BEGINNING OF THIS YEAR. HE COMPLAINED THAT THE QUARTERLY ALLOCATIONS FOR THE PRC DO NOT IN ANY WAY RESOLVE THIS MATTER AND THREATENED THAT FAILURE TO DO SOMETHING ABOUT THE PENDING CONTRACTS COULD AFFECT FUTURE US-CHINA BUSINESS. END SUMMARY.

1. AS PROPOSED REFS B AND C, USLO OFFICER HOROWITZ ON NOVEMBER 12 MET WITH FANG HSIN-MIN, IMPORT MANAGER OF THE CHINA NATIONAL METALS AND MINERALS IMPORT AND EXPORT CORPORATION (MINMETALS), TO DISCUSS FOURTH QUARTER EXPORT ALLOCATIONS OF STEEL SCRAP FOR THE PRC.

2. IN OPENING PRESENTATION, HOROWITZ RECALLED CONVERSATIONS ON STEEL SCRAP WITH FANG EARLIER THIS YEAR (PEKING 419  
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AND 476) WHEN HE EXPLAINED THE REASONS FOR

THE EXPORT CONTROLS AND HOW THE PROGRAM OPERATES. HE THEN REFERRED TO RECENT DISCUSSIONS IN WASHINGTON (REFS A AND C), AND EXPLAINED TO FANG THE FOURTH QUARTER REGULAR AND CONTINGENCY ALLOCATIONS FOR PRC, STRESSING THE GREATER FLEXIBILITY IN CURRENT RULES AS COMPARED TO THE FIRST QUARTER OF THE YEAR. HE ALSO PROVIDED FANG WITH A TYPE-WRITTEN SUMMARY OF THE HIGHLIGHTS OF THE FOURTH QUARTER ALLOCATIONS AND WITH A COPY OF EXPORT ADMINISTRATION BULLETIN NO. 124.

3. RELYING MOSTLY ON PREPARED NOTES, FANG MADE A FAR MORE FORCEFUL STATEMENT OF THE CHINESE POSITION THAN HE HAD GIVEN IN MEETINGS WITH USLO OFFICERS EARLIER THIS YEAR. AFTER THANKING HOROWITZ FOR THE INFORMATION PRESENTED, HE SAID MINMETALS HAS REPEATEDLY ASKED THOSE US FIRMS WHICH ARE PARTIES TO THE UNFULFILLED CONTRACTS TO EXECUTE THEM IN FULL AND IN ACCORD WITH ALL THEIR PROVISIONS. HE REITERATED THE IMPORTANCE OF RESPECT FOR CONTRACTS, AND SAID THAT BECAUSE OF THE FAILURE OF AMERICAN COMPANIES TO PERFORM, MINMETALS HAS SUSTAINED "VERY BIG LOSSES" AND THE END-USERS IN CHINA ARE COMPLAINING BITTERLY. THOSE CONTRACTS, HE SAID, COVER ALMOST 500,000 TONS OF SCRAP, AND ALTHOUGH SIGNED NEARLY A YEAR AGO, NOT A SINGLE TON HAS BEEN DELIVERED.

4. FANG SAID THERE IS A VERY IMPORTANT POINT OF PRINCIPLE INVOLVED AND MINMETALS WONDERS WHO IS RESPONSIBLE FOR THESE BREACHES OF CONTRACT. THE US COMPANIES INVOLVED ALL BLAME THE USG, HE SAID, AND IF SO, THIS DOES NOT CONFORM TO THE SPIRIT OF THE SHANGHAI COMMUNIQUE. LARGE TONNAGES AND AMOUNTS ARE INVOLVED; IT IS A BIG PROBLEM WHICH NEEDS TO BE SETTLED QUICKLY; OTHERWISE, HE WARNED, IT COULD "TO A VERY LARGE EXTENT PRODUCE ADVERSE AFFECTS ON US-CHINA BUSINESS NEGOTIATIONS." (FANG REPEATED THIS SENTENCE TO HIS INTERPRETER TO BE SURE THAT IT WAS CAREFULLY TRANSLATED.) THE PROBLEM, FANG CONTINUED, CANNOT BE RESOLVED BY THE PROVISION OF "NOMINAL" TONNAGES UNDER THE EXPORT QUOTA SYSTEM. TO CONSIDER SUCH SMALL QUANTITIES AS TAKING THE PLACE OF THE UNDELIVERED AMOUNTS WOULD BE NOTHING MORE THAN A "DISGUISED FORM OF BREACH OF CONTRACT." "THIS CONFIDENTIAL

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IS ENTIRELY UNACCEPTABLE TO US," FANG SAID. WE MUST STILL INSIST, HE WENT ON, THAT THE CONCERNED US FIRMS SUBMIT TO MINMETALS PROPOSALS AS TO HOW THEY WILL EXECUTE THEIR FULL OBLIGATIONS UNDER THE EXISTING CONTRACTS. ANYTHING THE USG CAN DO TO HASTEN SETTLEMENT OF THIS PROBLEM WOULD BE APPRECIATED, HE CONCLUDED.

5. IN RESPONSE, HOROWITZ REVIEWED AGAIN THE CIRCUMSTANCES

WHICH REGRETTABLY MADE IT NECESSARY FOR USG TO IMPOSE EXPORT CONTROLS ON STEEL SCRAP, AND THE EFFORTS MADE TO EMPLOY A SYSTEM THAT WOULD TREAT ALL US CUSTOMERS EQUITABLY. HE NOTED THAT AT THE TIME THE CONTRACTS IN QUESTION WERE NEGOTIATED, IT WAS WELL KNOWN THAT SOME SYSTEM OF EXPORT CONTROLS WOULD LIKELY BE IMPOSED AND WE CAN ONLY ASSUME THAT THE AMERICAN COMPANIES MADE IT CLEAR THAT DELIVERIES MIGHT BE SUBJECT TO EXPORT LICENSING. IN ANY CASE, HE SAID, THE USG CANNOT FORCE PRIVATE COMPANIES TO FULFILL CONTRACTS; PROBLEMS RELATING TO CONTRACTS NEED BE SETTLED EITHER IN THE COURTS OR BY THE PROCESS OF ARBITRATION AS PROVIDED IN THE CONTRACTS. MOREOVER, HE EXPLAINED, AN EXCEPTION FOR ONE COUNTRY, ESPECIALLY WHEN SUCH LARGE QUANTITIES ARE INVOLVED, WOULD DEFEAT THE PURPOSE OF THE CONTROLS AND UNDERMINE THE EFFORT TO BE FAIR TO ALL BUYERS OF US SCRAP. HE SAID HE HOPED THE CHINESE SIDE WOULD UNDERSTAND THESE CIRCUMSTANCES, AND THAT IT WILL BE POSSIBLE TO PROCEED WITH ORDERLY TRADE WITHIN THE FRAMEWORK OF THE EXPORT CONTROL SYSTEM THAT HAS BEEN SET UP.

6. IN THE ENSUING DISCUSSION MOST OF THE ABOVE ARGUMENTS WERE REVIEWED SEVERAL TIMES, BUT FANG WAS LESS POINTED ABOUT THE POSSIBLE EFFECTS OF THE PROBLEM ON FUTURE US-CHINA BUSINESS NEGOTIATIONS. HE SEEMED BE SAYING THAT MINMETALS WILL NOT DO FUTURE BUSINESS WITH THOSE COMPANIES WHICH ARE PARTIES TO THE UNFULFILLED CONTRACTS. THE MEETING ENDED AMICABLY, WITH FANG EXPRESSING APPRECIATION FOR HOROWITZ' CALL.

7. COMMENT: FANG'S MESSAGE IS LOUD AND CLEAR: THE FOURTH QUARTER CONTINGENCY ALLOCATION AND THE INCREASED FLEXIBILITY IN THE PROGRAM (REGARDING CHOICE OF US EXPORTERS) IS NOT CONFIDENTIAL

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ENOUGH AND SIMPLY DOES NOT SOLVE THE PROBLEM OF THE OUTSTANDING CONTRACTS. HIS STRESS, HOWEVER, ON MINMETALS DESIRE TO HEAR SOME PROPOSALS FROM THE CONCERNED US FIRMS MAKE US WONDER WHETHER THOSE FIRMS MIGHT NOT SEEK SOME NEGOTIATED SETTLEMENT WHICH WOULD INVOLVE SOME SUBSEQUENT SHIPMENTS WITHIN THE FRAMEWORK OF QUARTERLY ALLOCATIONS. WE ARE THINKING OF SOME KIND OF ARRANGEMENT ALONG THE LINES SUGGESTED IN PEKING 1559. AT THE SAME TIME, WE UNDERSTAND THAT ONE OR TWO US FIRMS AT THE CANTON FAIR TALKED TO THE CHINESE ABOUT SCRAP AND, ALTHOUGH NOT PRIVY TO DETAILS, WE WONDER IF MINMETALS IS CONSIDERING BUYING US SCRAP UNDER THE QUARTERLY QUOTA FROM FIRMS WHICH ARE NOT PARTIES TO THE UNFULFILLED CONTRACTS. ANY INFORMATION THE DEPARTMENT MAY HAVE ON THIS WILL BE APPRECIATED.  
BUSH

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